Supreme Court of the United States

October Term, 1923.

No. 266.

AIR-WAY ELECTRIC APPLIANCE CORPORATION,
Appellant,

vs.

HARRY S. DAY, TREASURER OF THE STATE OF OHIO, ET AL.,
Appellees.

No. 267.

HARRY S. DAY, TREASURER OF THE STATE OF OHIO; JOSEPH T. TRACY, AUDITOR OF THE STATE OF OHIO; JOHN R. CASSIDY, S. E. FORNEY, C. A. HORN, AS THE TAX COMMISSION OF THE STATE OF OHIO; AND THAD H. BROWN, SECRETARY OF STATE OF THE STATE OF OHIO,
Appellants,

vs.

AIR-WAY ELECTRIC APPLIANCE CORPORATION,
Appellee.

Appeals from the District Court of the United States for the Southern District of Ohio.

BRIEF FOR APPELLEES IN CASE No. 266 and for APPELLANTS IN CASE No. 267.

BRIEF FOR APPELLEES (STATE OFFICERS) IN CASE NO. 266.

STATEMENT OF THE CASE.

We adopt the statement given in the brief for appellant, except as supplemented by the following:

(A) The action taken as to plaintiff's stock by the department of securities is described in the bill of complaint in these words (Record, pp. 2 and 3):

> "The plaintiff corporation received a certificate from the department of securities of the State of Ohio **authorizing the sale** of its common and founders' stock at a price of seven dollars per share for **each share** of stock. * * *." (Black face ours.)

The answer of the state officers recites (Record, p. 11):

> "Defendants further admit that by act of the securities department under the so-called Blue Sky Law and upon the application of the plaintiff, the price at which said plaintiff was **permitted to offer** its stock for sale **in the state of Ohio** was seven dollars per share * * *." (Black face ours.)

The so-called securities or Blue Sky Law of Ohio (Sections 6373-1 to 6373-24, General Code of Ohio), entitled at the time of its original passage in 1913 (103 Ohio Laws, 743),

> "An act to regulate the sale of bonds, stocks and other securities and of real estate not located in Ohio, and to prevent fraud in such sales,"

provided among other things at the time plaintiff re-

ceived its said certificate, that corporations not exempted by the terms of the act from compliance therewith should, before selling their stock, or offering it for sale, in Ohio, file with the commissioner of securities an application for authority to make such sale, accompanied by certain specified information, and that (Sec. 6373-16):

> "* * * And if it shall appear that the law has been complied with and that the business of the applicant is not fraudulently conducted, and that the proposed disposal of such securities or other property is not on grossly unfair terms, and that the issuer or vendor is solvent, upon the payment of a fee of ten dollars the commissioner shall issue his certificate to that effect authorizing such disposal. * * * *"

Section 6373-17 then provided:

> "Such certificate shall recite in bold type that the 'commissioner' in no wise recommends such securities or other property; and no person or company shall advertise, in connection with the sale of such securities, the fact that such certificate has been issued unless such advertisement also contains in bold type a copy of such recital."

(B) Sec. 8728-11, Ohio G. C., the statute under attack, was first enacted in 1919. Through error in printing, the year is given as 1909, in the opinion of the District Court (Record, top p. 35). By way of addition to the statement of the District Court, it is perhaps proper to say that the act of 1919 (Secs. 8728-1 to 8728-12, Ohio G. C.), marked not only the beginning of legislation in Ohio authorizing the incorporation in that state of corporations with no par stock, but also contained in said

Section 8728-11 the first specific statutory provision for franchise taxes upon no par stock foreign corporations as distinguished from like corporations having par stock. The first amendment of the 1919 no par stock act was by the act of February 4th, 1920 (Rec., top p.35). This amendment is by error referred to in the brief of appellant (p. 5) as the amendment of February, 1919.

(C) The Delaware statute authorizing corporations to issue no-par stock is Section 1918 a, originally enacted as Section 4a of an act of March 20th, 1917 (Laws of Delaware, 1917, page 321):

> "1918a. Section 4a. **Stock Without Par Value.**—Any corporation may, if so provided in its certificate of incorporation or in an amendment thereof, issue shares of stock (other than stock preferred as to dividends or preferred as to its distributive share of the assets of the corporation or subject to redemption at a fixed price) without any nominal or par value. Every share of such stock without nominal or par value shall be equal to every other share of such stock, except that the certificate of incorporation may provide that such stock shall be divided into different classes with such designations and voting powers or restriction or qualification thereof as shall be stated therein, but all such stock shall be subordinate to the preferences given to preferred stock, if any. Such stock may be issued by the corporation from time to time for such consideration as may be fixed from time to time by the board of directors thereof, pursuant to authority conferred in the certificate of incorporation, or if such certificate shall not so provide, then by the consent of the holders of two-thirds of each class of stock then outstanding and entitled to vote given at a meeting called for that purpose in such manner as shall be prescribed by the by-laws, and any and all such shares so issued, the full consideration for which has

been paid or delivered, shall be deemed full paid stock and not liable to any further call or assessment thereon and the holder of such shares shall not be liable for any further payments under the provisions of this chapter.

In any case in which the law requires that the par value of the shares of stock of a corporation be stated in any certificate or paper, it shall be stated, in respect of such shares, that such shares are without par value, and wherever the amount of stock, authorized or issued, is required to be stated, the number of shares authorized or issued shall be stated, and it shall also be stated that such shares are without par value. For the purpose of the taxes prescribed to be paid on the filing of any certificate or other paper relating to corporations and of franchise taxes prescribed to be paid by corporations to this state, but for no other purpose, such shares shall be taken to be of the par value of one hundred dollars each."

ARGUMENT.

I.

The only function of the department of securities is to prevent the fraudulent sale of securities. If that function is to be enlarged, for the purposes of this case, to the extent claimed throughout the brief for appellant, then, logically, appellant's stock is worth $2,800,000.00, or seven dollars per share for the whole 400,000 shares.

II.

It is true, as stated in branch 6 of brief for appellant, (p. 37), that the answer of the state officers admits (Rec. top p. 15) that the amendment of Sec. 8728-11 did not go into effect until August 14, 1921. But accompanying the admission is a statement exhibiting the view of defendants that the amendment would not operate retroactively if applied in calculating plaintiff's tax for 1921. At best, the admission cannot be taken as one of fact, and is to be treated as a legal conclusion, since the determining factor is whether the operation of the amendment was held in abeyance for ninety days because of the referendum provision of the Ohio Constitution. This question is fully gone into by the District Court (Opinion, Rec., pp. 36 to 38); and the court holds that the amendatory act, being a revenue measure, went into immediate effect on its filing with the secretary of state on May 17th, 1921.

With these comments, we submit the case on the two opinions of the District Court, as set out at pages 34 and 51, respectively, of the record. The first of these opinions has been reported in 279 Federal Reporter, 878.

BRIEF FOR APPELLANTS (STATE OFFICERS) IN CASE No. 267.

STATEMENT OF THE CASE.

All of the manufacturing of Air-Way Electric Appliance Corporation is done in Ohio. (Rec., pp. 2, 24, 25). The total sales of the corporation during the eleven months it had been in business prior to June 30th, 1921, as of which latter date its annual report was made, amounted to $250,594.58, of which $179,792.28 was for sales outside of Ohio, and $70,802.30 was for sales in Ohio. (Affidavit, Rec., pp. 22, 23; affidavit, Rec., pp. 26, 27). The amounts thus given correspond to what complainant designated as business transacted outside of Ohio, and business transacted in Ohio, respectively, in its application to the tax commission to re-figure its tax (Rec., p. 19), and in its amendment and supplement to bill of complaint (Rec., p. 16).

The figures just noted were taken by the District Court as representing plaintiff's "business transacted" outside of Ohio, and within Ohio, respectively, and were accordingly used by that court in calculating the tax, all as shown by the following excerpt from the court's opinion (Record, pp. 53 to 55):

> "In the case of Hump Hairpin Mfg. Co. v. Emmerson, supra, it was held that the business done by a corporation, similarly situated to the plaintiff in this case, with residents of states other than Illinois, is interstate business, and that a state may not use its taxing power to regulate or burden intertate commerce. However, it was concluded in that case that 'at the most, the assessment is, so far as interstate commerce is concerned, incidental, remote and

unimportant, and it is therefore constitutional.' In the instant case, the amount assessed by the commission upon interstate commerce is not remote, incidental and unimportant, but, on the contrary, is a substantial sum levied directly upon the stock representing interstate business. It is wholly unnecessary to consider the power of a state to levy a tax in gross upon a foreign corporation based upon the company's entire business both intrastate and interstate, for as we construe this statute it was not the purpose and intent of the general assembly of Ohio to include interstate business as a basis for this levy but only as a factor in determining the proportion that should be paid upon strictly state business. The purpose and intent of this statute is further discussed later in this opinion. But wholly aside from this consideration, it is clear from admitted facts, which were not before the tax commission when the assessment in question was made and certified, that the commission has not applied its own announced rule for the ascertainment of the correct amount of tax to be paid by foreign corporations. The plaintiff is manifestly entitled to the benefit of that rule and it must be presumed the tax would have been computed in accordance therewith, if the report of plaintiff to the tax commission had correctly and fully disclosed the facts pertaining to its business. That the commission finally failed to do so through mistake or inadvertence is no reason for denying relief from an erroneous charge. Cooley on Taxation, 1447; Charleston v. County Com'rs., 109 Mass., 270; Dunnell Mfg. Co. v. Inhabitants of Pawtucket, 73 Mass. 277; City of Wilmington v. Ricaud, 90 Fed. 214, C. C. A. 4; Brown v. French, 80 Fed. 166.

From the pleadings and evidence the amount of plaintiff's authorized common stock represented by property owned and used and business transacted in the state is readily ascertainable. Having regard to the teachings of the Hump Hairpin Mfg. Company case, which is necessarily controlling, if the amount

of plaintiff's property in Ohio ($458,278.56) plus the amount of its business in Ohio ($70,802.30) be divided by the amount of its property in Ohio ($458,-278.56) plus its total business transacted ($250,-594.58), the resulting quotient multiplied by the number of shares of authorized common stock gives the number of shares (298,520) representing the property owned and used and business transacted in this state. The computation thus made coincides with the result obtained by the use of the formula specifically set forth at pp. 156, 157, in the Ohio Tax Laws compiled by the tax commission in 1920, by the use of which it is said 'the amount of tax to be assessed under the statute may be worked out with mathematical precision.' The tax on 298,520 shares at five cents per share is $14,926.00—the amount which plaintiff should pay, if there be no valid ground for relief from any part of the same.

It is true that following the above mentioned formula promulgated by the tax commission is a statement (p. 157) expressing the conclusion reached by the attorney general of Ohio in 1915 (Attorney General's Report, 1915, p. 460), that 'The operation of a factory in Ohio by a foreign corporation having its principal place of business in another state constitutes 'doing business' in Ohio, regardless of where the products of such factory are sold or transported; and it is reasonable and lawful under Sec. 5502 to measure the volume of such business by sales of manufactured articles, whether such sales otherwise represent interstate commerce or not.' Sec. 5502 relates to the determination by the tax commission of the proportion of the authorized capital stock of a foreign corporation represented by its property and business in the state and the certification of the same to the auditor of state. If in determining the amount of the state excise tax the use made of the amount of sales representing interstate business is such that the tax affects interstate commerce so directly and immediately as to constitute

a genuine and substantial burden or restraint upon such commerce, the view expressed in the above quoted passage is under the rule announced in the Hump Hairpin Mfg. Company case unusual, and, if the statute here under consideration is in its general operation productive of such a result it must fail for want of constitutionality. The annual tax assessed against a foreign corporation is, it is true, for the privilege of exercising its franchises in the state, but the interstate business being a factor in measuring the amount, if the tax be excessive on account of such factor, the net result is the substantial and genuine fettering of such business."

The $14,926.00 thus arrived at is the amount for which the District Court rendered its decree.

ASSIGNMENT OF ERRORS.

(Record page 67.)

"Said court erred in finding that 298,520 shares of the authorized capital of plaintiff represented the property owned and used and business transacted by plaintiff in the state of Ohio, and in not finding a greater number of such shares * * * to represent the property owned and used and business transacted by plaintiff in the state of Ohio."

"Said court erred in finding plaintiff's tax to be $14,926.00, and in not finding said tax to be in excess of such sum * * *."

"Said court erred in enjoining the tax commission of Ohio from certifying for collection the nonpayment by plaintiff of a tax in excess of $14,926.00, and in enjoining the secretary of state, auditor of state and treasurer of state, of the state of Ohio, from collecting or attempting to collect any part of a tax in excess of $14,926.00, * * *."

ARGUMENT.

"Business Transacted" in Ohio by a Foreign Corporation Doing all its Manufacturing in Ohio and Selling its Products Both in and Outside of Ohio, Includes, Within the Contemplation of Sections 5499 to 5503, General Code, the Entire Manufacturing Cost of Such Products.

Sections 5499 and 5503 are quoted in the brief for appellant (pp. 4 and 5). We quote here Sections 5501 and 5502:

"**Sec. 5501.** Such report shall contain:

1. The name of the corporation and under the laws of what state or country organized.

2. The location of its principal office.

3. The names of the president, secretary, treasurer and members of the board of directors, with the post-office address of each.

4. The date of the annual election of officers.

5. The amount of authorized capital stock, and the par value of each share.

6. The amount of capital stock subscribed, the amount of capital stock issued, and the amount of capital stock paid up.

7. The nature and kind of business in which the company is engaged and its place or places of business, both within and without the state.

8. The name and location of its office or offices in this state, and the name and address of the officers or agents of the corporation in charge of its business in this state.

9. The value of the property owned and used by the company in this state, where situated, and the value of the property owned and used outside of this state, and where situated.

10. The change or changes, if any, in the above particulars made since the last annual report."

"**Sec. 5502.** Upon the filing of the report, provided for in the last three preceding sections, the commission, from the facts thus reported and any other facts coming to its knowledge, bearing upon the question, shall, on the first Monday in September, determine the proportion of the authorized capital stock of the company represented by its property and business in this state. On the first Monday of October, the commission shall certify the amount of the proportion of the authorized capital stock of each such company represented by its property and business in this state, as determined by it, to the auditor of state."

The construction of Sections 5499 et seq., which we here contend for, was not presented to the District Court. There is no finding of facts by that court, nor is there any evidence, showing manufacturing costs. Nevertheless, we take it that if this court finds that the decree below proceeded from an erroneous view of the law, there may be a reversal with instructions to the District Court to make correction in the amount of the tax.

Murdock v. Ward, 178 U. S., 139; 149.
Little Miami Railroad Company v. United States, 108 U. S., 277.
Barnes v. Williams, 11 Wheaton, 415.

The exceedingly small element of interstate commerce in a case like the present, was pointed out in **Hump Hair Pin Mfg. Co. v. Emmerson**, 258 U. S., 290.

But we have been unable to discover anything in that case or in the formula of the tax commission referred to by the District Court which excludes from the term "business transacted in Ohio" the cost of manufacturing in Ohio of goods which might ultimately be sold in interstate commerce. The formula of the tax commission is a verbatim quotation from the case of **State of Ohio v. Cabin Creek Consolidated Coal Company**, 17 Ohio Nisi Prius Reports (New Series), page 60, and we quote the formula in full (Ohio Tax Laws, 1920, as compiled by the tax commission):

> "The tax commission is an administrative body, being required to determine the tax 'upon the proportion of the authorized capital stock of the corporation represented by the property owned and used and business transacted in this state.' (Section 5502.) Its function is to follow the letter of the statute and make the mathematical computation according to the intent thereof.
>
> By so doing, the amount of tax to be assessed under the statute may be worked out with mathematical precision as follows:

Value of property in Ohio	$ 300.00
Business done in Ohio	138,752.28
Total	$139,052.28
Value of property in West Virginia	$2,470,400.00
Business done outside of Ohio	737,074.58
Total	$3,207,474.58
Total property and business both in and outside of Ohio	$3,346,526.58

139,052÷3,346,526=.04155
$1,500,000x.04155=$62,225
Authorized capital stock stock $1,500,000.

Three-twentieths of one per cent. of $62,225=$93.337"

The opinion of the attorney general of Ohio mentioned by the District Court (Opinions of the Attorney General for 1915, Vol. 1, p. 460) dealt with a foreign corporation which had its principal place of business and actual business office in Illinois and had various manufacturing plants located both in Ohio and outside of Ohio. It was as to such a corporation that the attorney general held that the total sales from the Ohio manufacturing plants might be taken as the criterion of "doing business" in Ohio, regardless of whether the products were sold in Ohio or elsewhere. But neither that opinion nor the formula of the tax commission undertakes to define "business transacted in Ohio" as applied to such a case as the present, where the entire manufacturing is done in Ohio and the actual business office is in Ohio.

We submit then that the District Court was not warranted in treating plaintiff's sales, $179,792.28, outside of Ohio as "business transacted" outside of Ohio, but that from such amount there should be deducted the cost of manufacturing.

This construction of the statute, we submit, will not yield an unconstitutional result as burdening interstate commerce;

American Manufacturing Co. v. City of St. Louis 250 U. S., 459;
The Minnesota Rate Cases, 230 U. S., 352; 411.
Bacon v. Illinois, 227 U. S., 504.
Coe v. Errol, 116 U. S., 517.

And again, the construction is consistent with the principle that goods do not enter the field of interstate commerce until they begin to be transported to another state from the state in which they were manufactured.

Kidd v. Pearson, 128 U. S., 1.
Cornell v. Coyne, 192 U. S., 418.
Diamond Glue Co. v. United States Glue Company. 187 U. S., 611.
McCluskey, Admr. v. Marysville, etc. R'y Co., 243 U. S., 36.
Coe v. Errol, supra.
Bacon v. Illinois, supra.

CONCLUSION.

We submit, then, that the decree of the District Court should be reversed in so far as it limits the amount of the tax to $14,926.00, and should be affirmed in all other respects.

Respectfully submitted,

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